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SUBJECT: UKRAINE CURRENCY DOWN 20 PERCENT; RADA DIVIDED ON
SOLUTIONS

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11. (SBU) Summary. While Rada factions were busy haggling over three competing versions of anti-crisis measures, the hryvnia exchange rate slipped dramatically on October 23. Embassy contacts in the real estate and transportation sectors report more dismal news, indicating general woes throughout the real economy. End Summary.

Rada Not Equipped to Solve Financial Crisis

12. (SBU) Bickering in the Verkhovna Rada (reftel) has hampered efforts to pass anti-crisis legislation. All three major political factions support distinct programs, with Viktor Yanukovich's Party of Regions the latest to offer a (still undisclosed) proposal. Thus far, the Yushchenko-supported National Security and Defense Council (NSDC) anti-crisis measure and the Timoshenko-supported Cabinet of Ministers bill have been made public. While it is still too early to make a comparative analysis of the draft packages, it does appear that the NSDC and CabMin versions share an intention to bolster bank liquidity, increase deposit guarantees, and reduce growth rates in public sector wages, pensions, and social spending. We are already hearing that such spending cuts will face stiff challenges from Rada deputies across the political spectrum.

13. (SBU) Yushchenko noted that "every kopeck" spent should be "well thought-out," and he again blamed not the National Bank of Ukraine (NBU), but Tymoshenko's government for the crisis. Yushchenko insisted that he would even be willing to work with the Communist Party if it acted in the interests of the priorities of Ukraine, and that the legislative deadlock was a "tragedy."

Rapid Currency Devaluation

14. (SBU) The hryvnia (UAH)/dollar exchange rate has plummeted roughly 20 percent in the last twenty-four hours. Bid-ask quotes on the street ranged 5.86-5.95 (buying hryvnia) to 6.15-6.20 (buying dollars). Evening television news on October 22 reported that exchange kiosks were unable to sell dollars, due to the scarcity of foreign currency on the market. But when EconOff walked into separate kiosks on October 23, traders were not only able to sell dollars but very eager to do so.

15. (SBU) Other anecdotal evidence underlines how the exchange rate may be causing consumer prices to increase rapidly. A savvy, elderly woman selling flowers on the street was quoted as saying her 5-10% overnight price increases were due to the more expensive

dollar rate. Similarly, an open-air fruit stand owner said her supplier would increase wholesale prices by 3 percent on October 27. She was also told to be prepared for further increases thereafter, since most produce on the market is imported with prices sensitive to exchange rate devaluation.

¶6. (U) The NBU sold a limited number of dollars at 5.25 UAH/dollar to four commercial banks on October 22. According to the NBU, reserves have fallen 8.6 percent since October 1, due to infusions to prop up the currency and the banking sector. NBU Governor Volodymyr Stelmakh told reporters on October 22 that the central bank will continue to support the exchange rate.

Real Estate Markets Tanking

¶7. (SBU) Oleksandr Pochkun, Managing Partner of Baker Tilly International, the fifth largest accounting firm in Ukraine, briefed EconOff on the effects of the financial crisis for his key corporate clients. In particular, he stated that construction projects and property markets, where commercial real estate holders are exposed in varying degrees to Ukraine's financial crisis, have grinded to a standstill. Large-scale commercial real estate developers face the greatest risks, since they lack funding for further construction and have invested nearly all their cash into land holdings that were to have been sporadically sold for revenue. Pochkun estimated that without loan injections, some major developers face bankruptcy, as they hold less than three months' cash to meet payroll and will be unlikely to find buyers for some of their largest holdings on the open market.

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¶8. (SBU) Major Ukrainian oligarchs with urban land holdings likewise face pressure from declining steel and commodity prices. One source told us that 21st Century investments, a publicly traded real-estate company that purchased large tracts of land in Kyiv in the past year, was insolvent. Conglomerates may be looking to finance debt through property sales in the absence of available foreign capital. A sell-off of their holdings would have a dramatic effect generally on the real estate market, where Pochkun says there are already signs of panic. Access to credit has dried up, and individual speculators, who had bought one or two properties in addition to their primary residences, are now selling holdings faster than the market can absorb. He added that there is now a profound psychological element to the sell-offs, especially considering the fact that real estate investors had seen up to three-fold gains over the past two years.

Declines in Freight, Ports, Air Travel

¶9. (U) The unfolding financial crisis continues to hit other sectors of the economy. Ukrainian railroads and the country's ports have both reported significant drops in freight traffic in recent weeks. According to Ukraine's State Statistics Committee, freight transportation by sea and river links has decreased 14.6 percent thus far in 2008. The Odessa port authority commented that it has seen a significant drop in metals shipments, though increased grain exports have somewhat offset these declines. Oil reloading in Odessa has fallen as well, due to decreases in Russian-origin shipments. The state railroad company Ukrzaliznytsia reported a 20 percent drop in cargo transportation in October, due to decreased shipment of metallurgical and chemical products, iron ore, coal, and construction materials.

¶10. (SBU) An Embassy contact with ties to Mittal Steel Kryviy Rih, the country's largest steelmaker, recounted a conversation with the company's financial director, who said the vast plant was operating at 50 percent capacity, with large unsold inventories accumulating at the site. Yuri Miroshnikov, President of Ukraine International Airlines, and KLM/Air France Country Director Arvin Alagh told us that their airlines have seen a dramatic drop in advanced bookings for domestic and international flights. Executives of other

airlines echoed their statements at a recent roundtable sponsored by the American Chamber of Commerce. Airline representatives openly worried about general declines in air travel, and they suggested that their profits would be further hampered by high jet fuel prices that have not fallen in line with the price of crude oil. According to Aerosvit representatives, airlines in Ukraine have paying up to 40 percent above market rates due to reported price gouging by Lukoil, TNK/BP, and KreBo (Kremenchuk refinery/Borispol airport joint venture), forcing carriers to heavily refuel during European stopovers.

¶11. (SBU) Comment. Ongoing political animosities in the Rada aside, Ukraine's real economy has taken a strong downturn, as measured on the street in quotidian transactions and on corporate balance sheets. A rapid currency devaluation appears inevitable, and its effects are already taking a toll on everyday consumers and businesses. Proposals for anti-crisis legislation may be heard by parliament on October 24, but Ukrainians are not waiting for a political solution to take action in the market. End Comment.

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